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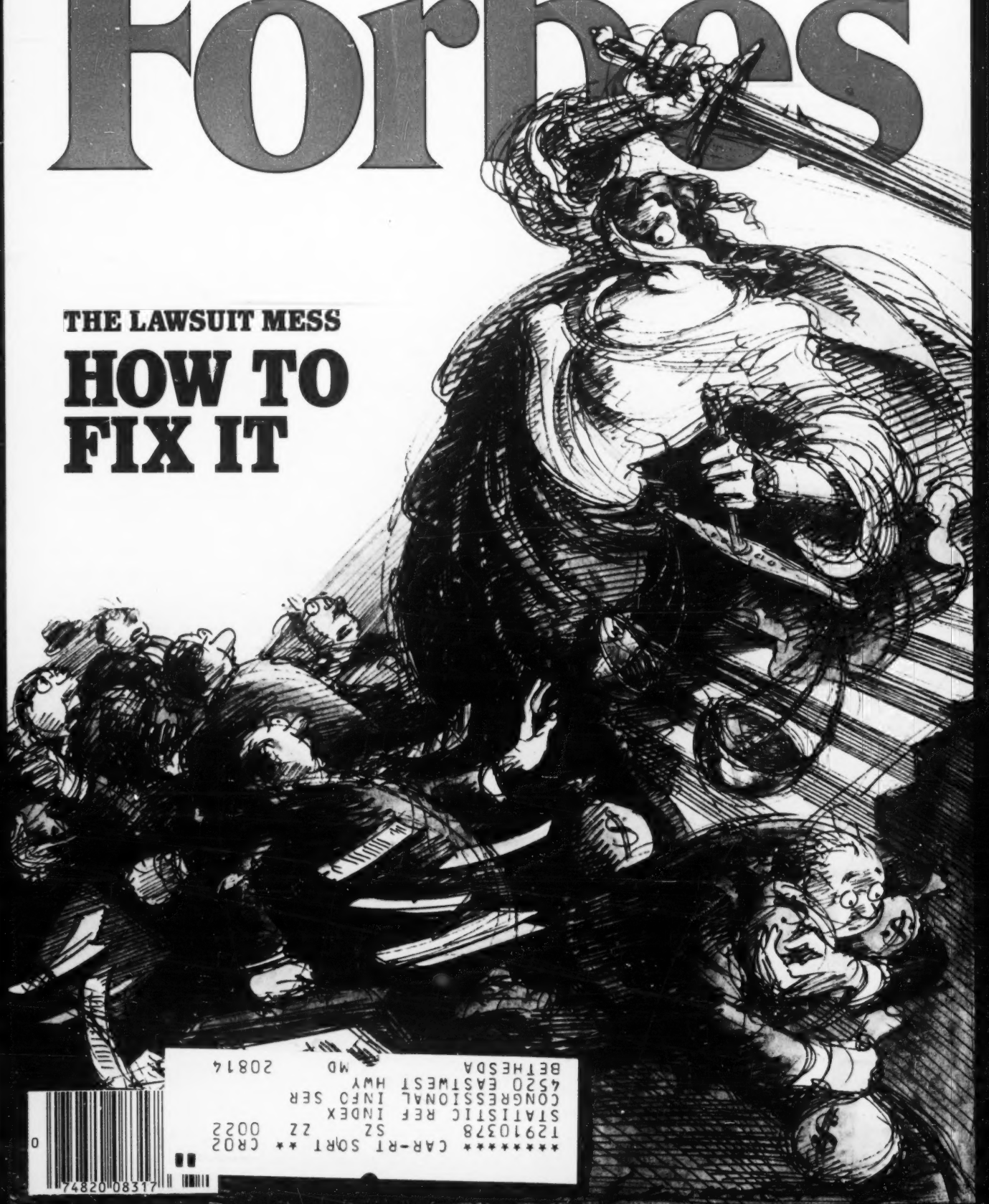

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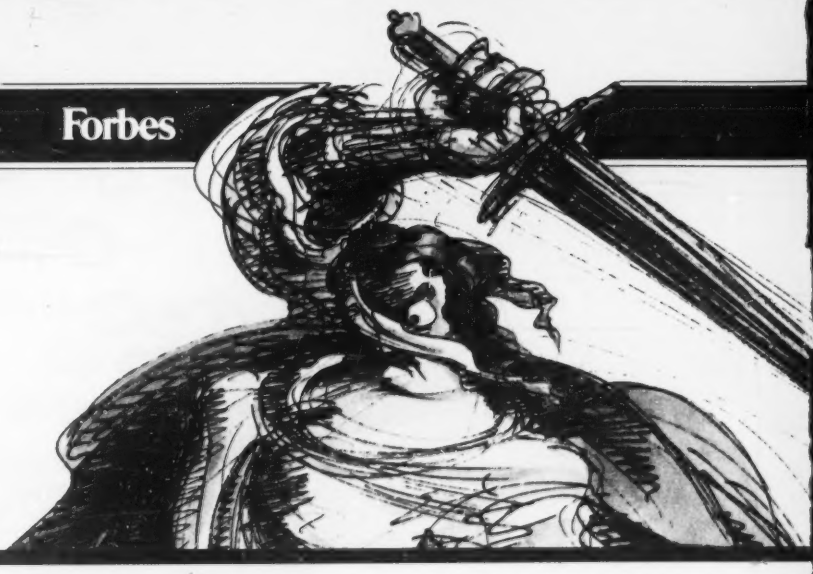

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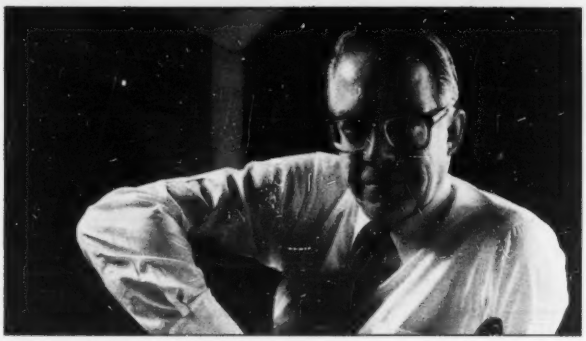

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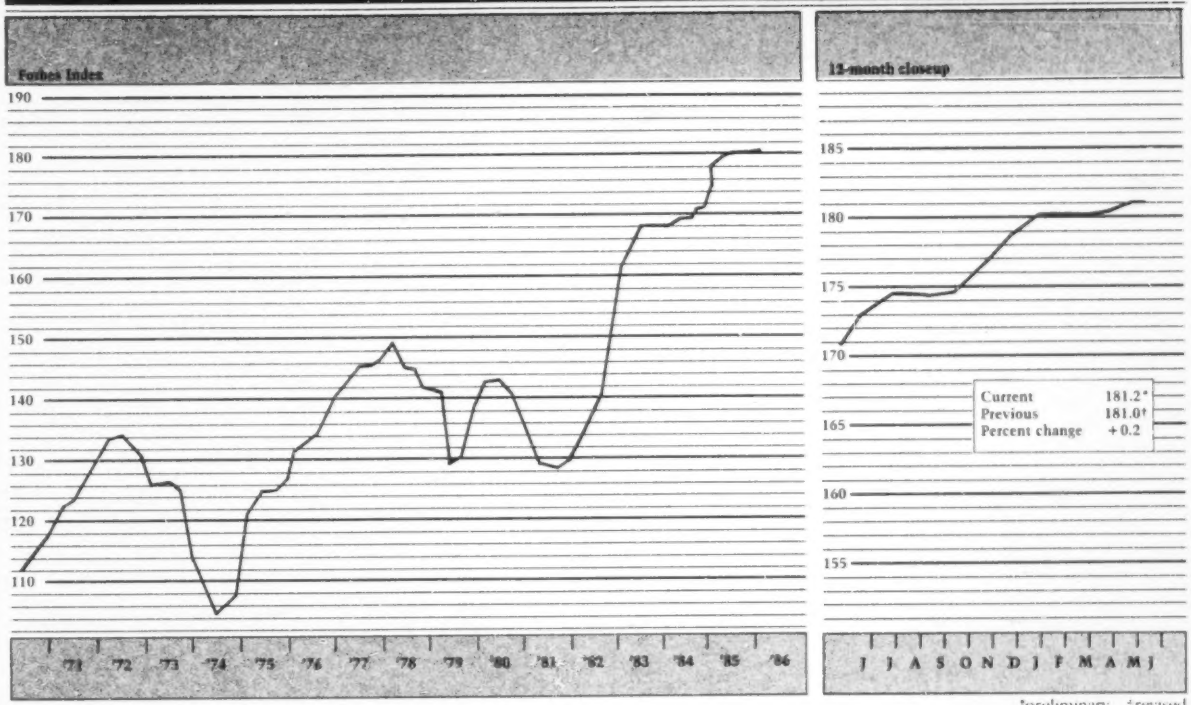
The Forbes Index



*preliminary †revised

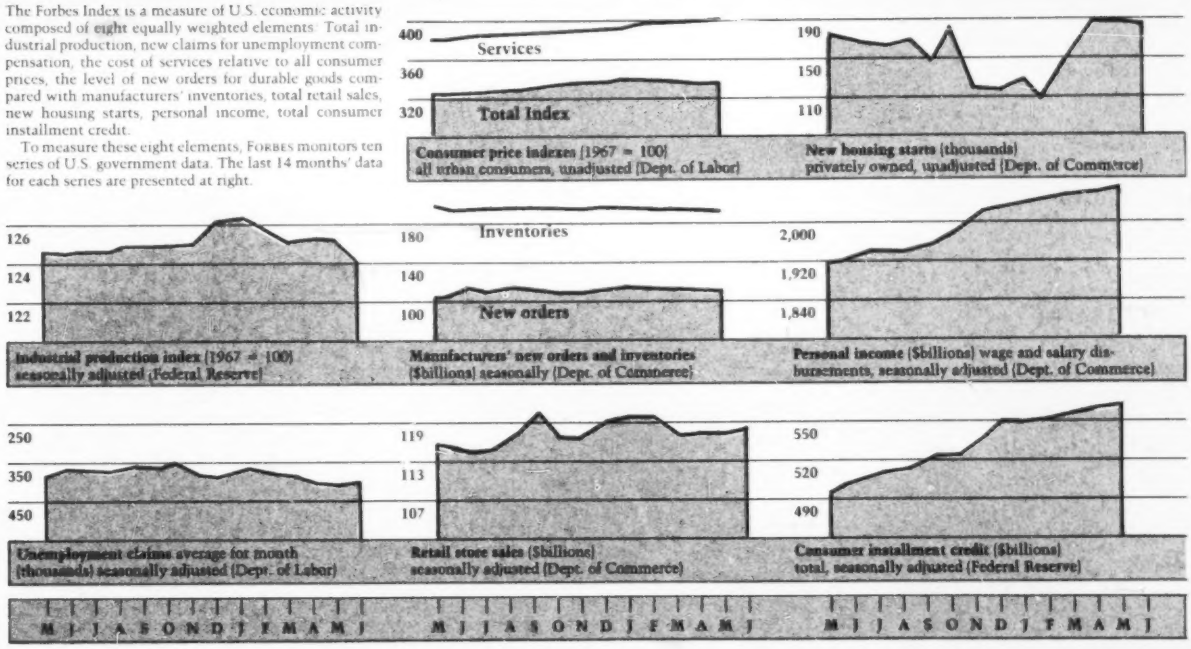
I.O.U. Thanks to the willingness of consumers to buy now and pay later, the Forbes Index eked out a 0.2% increase during the latest reporting period. The Index was given a boost by a 1% jump in consumer installment credit, which now stands 14.7% higher than it did the same time last year. A 0.2% rise in retail sales along with a 0.4% drop in new unemployment claims also pushed up the Index slightly.

Industrial production decreased by 0.5% during June. Almost half of the decrease, however, was related to strikes affecting the output of business equipment, construction supplies and durable materials. New housing starts fell 2% from May but were still 12.2% higher than they were one year ago.

The Forbes Index Components

The Forbes Index is a measure of U.S. economic activity composed of eight equally weighted elements: Total industrial production, new claims for unemployment compensation, the cost of services relative to all consumer prices, the level of new orders for durable goods compared with manufacturers' inventories, total retail sales, new housing starts, personal income, total consumer installment credit.

To measure these eight elements, FORBES monitors ten series of U.S. government data. The last 14 months' data for each series are presented at right.


400
360
320
Services
Total Index
Consumer price indexes (1967 = 100) all urban consumers, unadjusted (Dept. of Labor)
190
150
110
New housing starts (thousands) privately owned, unadjusted (Dept. of Commerce)
126
124
122
Industrial production index (1967 = 100) seasonally adjusted (Federal Reserve)
180
140
100
Inventories
New orders
Manufacturers' new orders and inventories ($billions) seasonally (Dept. of Commerce)
2,000
1,920
1,840
Personal income ($billions) wage and salary disbursements, seasonally adjusted (Dept. of Commerce)
250
350
450
Unemployment claims average for month (thousands) seasonally adjusted (Dept. of Labor)
119
113
107
Retail store sales ($billions) seasonally adjusted (Dept. of Commerce)
550
520
490
Consumer installment credit ($billions) total, seasonally adjusted (Federal Reserve)
M J J A S O N D J F M A M J
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Battling the Bell operating companies for choice cellular phone markets would be tough enough. The Federal Communications Commission has made it rougher.

Static on the line

By Ruth Simon

"WE INTEND TO STAY [in cellular], but it's getting awful lonely," says John Stanton, executive vice president of McCaw Communications Cos., now the largest cellular phone company outside the telephone, or wireline, industry.

Stanton isn't completely alone yet, but the ranks are thinning. The reasons are several. The Federal Communications Commission began by throttling non-wireline companies that were trying to get into cellular. The baby Bells would be powerful competitors even if the FCC hadn't handed them a head start in promising markets. And now, with sales estimates for the cellular industry as high as $2.6 billion by 1990, Bell companies have been paying record—some would say outlandish—prices to buy out their competitors. Southwestern Bell's $1.65 billion embrace of Metromedia's cellular and paging business is the latest example.

The FCC did not plan it this way. It says it was trying to encourage competition when it began handing out licenses to operate cellular, that is radio-telephone, systems on a two-per-city basis in 1983. To try to prevent a Bell monopoly, the FCC reserved one license for a telephone company, and the second for a non-wireline firm.

But the non-wireline companies were hamstrung from the start. Only the local phone companies could vie for the wireline license in each cellular market. With few competitors per city, the phone companies quickly divided their cellular franchises, began building systems, and were the first in most major markets to offer service. On the non-wireline end, competition was keener and the selection process cumbersome. The FCC awarded licenses in the 30 largest cities only after public hearings, and in smaller markets by lottery. Some awards were further delayed by legal challenges. Obvious to everyone but the FCC, this gave the wirelines a crucial head start. It also guaranteed that their competition would be fragmented and forced to make marriages of convenience, taking small shares of partnerships to better their odds.

Shotgun marriages make for poor relations, and some non-wireline partnerships have been hurt by con-

in a 35-knot crosswind

Rescue work at sea is seldom done in fine weather and calm seas. That's why the United States Coast Guard demands stringent requirements for their helicopters, including stability in flight – even in strong crosswinds – and protection against potential tail-rotor accident hazards.
To meet the Coast Guard's challenge Aerospatiale used its innovative "fenestron" technology. Advanced technology first introduced in the Gazelle in 1966, technology which has consistently proven performance, stability, safety and reliability.

This proven technology has caught the interest of the U.S. Army. The "fenestron" has been requested in the specifications for the Army's next generation helicopter... the LHX.
As we see it, advanced technology is synonymous with increased operational safety and reliability. This means adapting leading-edge technology to satisfy our customer's needs, which is one reason why the U.S.C.G. as well as fire departments, police units, hospitals, armed forces, and VIPs the world over place their trust in Aerospatiale... the world's leading helicopter exporter.

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flicts among their members. Others, seeing the prices they could command, simply sold out. And many who still fancy themselves to be long-term players are bailing out of markets where they have tiny shares to build majority stakes elsewhere.

"I don't need somebody telling me how to do things," explains Jack Brennan of Metro Mobile CTS, a privately held company controlled by the Bass brothers and Lindemann Enterprises that has sold small interests in Cincinnati and Houston. Brennan is drawing back to a hub-and-spoke strategy. He hopes to take advantage of administrative and marketing economies of scale by staying in cities clustered near one another, such as Phoenix, Tucson, El Paso and Albuquerque.

Metro Mobile isn't the only one. McCaw, a $78 million (sales) private company 45% owned by Affiliated Publications (publishers of the *Boston Globe*), recently agreed to pay $155 million for two small cellular companies that together control 11 southern cities. New York-based LIN Broadcasting (1985 sales, $172 million) has sold minority interests in Bridgeport and Hartford, Conn., while building its stake in Dallas and Houston.

But the Goliaths of the telephone industry are playing this game, too. In June, Southwestern Bell announced it would pay a record $1.65 billion—$41 per potential customer—for Metromedia's interests in such prime markets as Chicago, New York and Washington/Baltimore. The purchase followed a decision in February by Judge Harold Greene allowing Pacific Telesis Group, a Bell operating company, to purchase Communications Industries, a non-wireline with interests in San Francisco, Atlanta, San Diego and Dallas.

At more than twice the price cellular licenses traded for six months earlier, the Metromedia sale was one more indication of the telephone companies' superior financial strength. "A $1.6 billion transaction is beyond what we could reasonably afford to pay," admits Stanton, who had eyed the Metromedia properties. "We're moving toward an industry dominated by the telephone companies," he adds. "What am I going to do, tender for PacTel?"

With that kind of acquisition out of the question and the recent spate of Bell company purchases, the non-wirelines will soon be excluded from five major markets—Chicago, Boston, Baltimore/Washington, Atlanta and San Diego. In several others they are being forced into uncomfortable partnerships. Consider LIN Broadcasting. LIN's minority partner in Dallas is PacTel, its competitor in Los Angeles. Its Dallas competitor, Southwestern Bell, will soon be its partner in Philadelphia and New York.

PacTel has agreed to become a passive partner in Dallas, where it has a 16% stake. But Southwestern Bell will have close to a 50% stake in its new markets. "It's something we're going to have to be focusing on," admits LIN Vice President Michael Plouf. Like other non-wirelines, LIN has argued that the Bell purchases will reduce competition and slow the industry's development.

Major non-wireline cellular phone companies

Company	Largest cities served	Potential customers* (millions)
McCaw Communications	San Francisco, Pittsburgh, Minneapolis, Denver	25.6
LIN Broadcasting	New York, Los Angeles, Philadelphia, Dallas	16.2
Mobile Communications Corp of America†	Los Angeles, Houston, Milwaukee, Indianapolis	10.3
Metro Mobile CTS	Phoenix, Hartford, Providence, Bridgeport	8.5
Graphic Scanning	Detroit, St. Louis, Minneapolis, Cleveland	6.3

*Population in cities served according to 1980 census times share of license. †Joint venture with BellSouth awaiting regulatory approval.

Nubar Alexanian

John Stanton of McCaw Communications
"What am I going to do, tender for PacTel?"

The non-wirelines say they will provide better service and more aggressive pricing than traditional phone companies. But with their aggressive buyout strategies, the baby Bells have already shown their financial muscle. The oldest cellular system, Chicago's, is less than three years old, and because of licensing delays many non-wireline systems have gotten off the ground six months to nearly two years behind their competitors.

"Head start is thus far the major factor," says industry analyst Herschel Shosteck. In Baltimore/Washington, the 2½-year-old non-wireline group got out of the gate four months before Bell Atlantic did and now controls two-thirds of its market. In Chicago, where Ameritech, the Bell company, had a 15-month lead, the 1½-year-old non-wireline has only a 40% share.

To develop a customer base and name recognition while they build their own systems, most non-wirelines have chosen to resell cellular service purchased from the wirelines. It's a smart enough long-term strategy but adds to already heavy startup costs. "For every dollar the customer was spending, we were spending another dollar," says Metro Mobile's Brennan, who has invested $40 million to get his cellular systems up. "In Phoenix, we were losing $200,000 to $300,000 as a reseller per month." And even after their systems are up, the non-wirelines still have to buy connections into the landline telephone system from their wireline competitors.

With only 450,000 subscribers nationwide, many cellular systems are at least two years from profitability. Doesn't it make sense to take a profit now and sell out while licenses are trading at alltime highs? "We're on the verge of such an exciting, explosive period of growth," counters McCaw's Stanton, whose company has funneled about $400 million into cellular. "I don't believe there's a better investment in America today."

Certainly with prices for licenses going into the stratosphere, lots of folks are already making wads of dough in the cellular phone business. But the FCC's heavy hand seems also to have shaped an industry where the Bell companies are getting the biggest piece of the pie. ■

Buried in the balance sheet of a sleepy old water company that once had P.T. Barnum as its president is some of the most desirable real estate in the Northeast.

Found money

By Allan Dodds Frank

WATER COMPANIES. Predictable earnings, just the thing for widows, orphans and the over-the-thrill crowd. Not any longer. In keeping with the deal-a-minute spirit of the times, investor-owned electric utilities around the country have begun diversifying into everything from drugstore chains to cable TV and even banking—and now water utilities have begun to follow suit.

When companies diversify, they usually pay for it by either issuing securities or drawing down cash. Rare is the firm that is able to launch itself into a whole new business by simply selling off assets at maybe 100 times the value at which they are carried on the firm's books. That, however, is precisely the plan of The Hydraulic Co., the largest investor-owned water utility in Connecticut.

For more than 100 years, THC (long known as Bridgeport Hydraulic) has been earning modest but predictable profits by supplying water to customers of southwestern Connecticut—an activity about as exciting as the embalming business. But the company also owns 20,000 acres, nearly all prime residential real estate. Some of it was acquired as long ago as the 1880s by the utility's second chief executive, showman Phineas T. Barnum, as reservoir watershed land at less than $1,000 per acre. As it happens, the land is situated in the heart of Fairfield County, a gilt-edged real estate market in which choice lots go for $100,000 apiece or much more.

Some 2,200 acres of that property is what THC wants to begin selling, and if approval comes for an initial offering, requests for further sales are almost sure to follow. THC is joining a growing number of utilities diversifying from regulated into nonregulated businesses, such as real estate development. In northern New Jersey, United Water Resources is using its Rivervale Realty subsidiary to develop nearly 1,000 acres in surrounding communities that it bought from another subsidiary, venerable Hackensack Water Co. As part of the deal, Hackensack Water split the proceeds 50/50 with rate payers, giving each customer an $18 check and the rest to the parent. By contrast, Hydraulic is seeking to convince Connecticut authorities to change a state regulation requiring any return on water company real estate sales to be rebated 100% to utility customers in the form of lower rates. Hydraulic wants permission to keep two-thirds of the real estate proceeds, with one-third going to rate payers.

In a low-key but top-priority campaign to free itself of the existing restrictions, THC in April petitioned the Connecticut Department of Public Utility Control for what amounts to blanket permission to sell any land the company can convince Connecticut authorities to declare surplus. An initial ruling on the matter could come as early as mid-August, and could well affect all of Connecticut's 130 investor-owned water companies.

The heart of the Hydraulic system is Easton, where nearly 40% of the town's 28 square miles is owned as watershed land by THC. Lying at the edge of the commuting suburbs of New York City, 60 miles to the southwest, Easton has not permitted any commercial or industrial development, and restricts nearly all zoning to 3-acre minimum lots. The result: an exclusive, bucolic woodland community in which homes begin at $200,000 and climb into the millions.

Many local residents vigorously oppose THC's plans. If the utility is allowed to develop its land to the maximum feasible, the result could arguably be to add perhaps as many as 2,000 homes to the area, changing the rural nature of the entire region. THC claims it wants to sell off the 2,200 acres—raising, FORBES estimates, perhaps $100 million or more—to pay for the construction of two filtration plants. Yet the plants would further reduce the need for watershed acreage, opening additional land to be declared surplus, and then perhaps sold. First Selectman Mary Anne Guitar of the town of Redding, which contains vast THC watershed acreage, opposes the plan: "We figure it is like eating peanuts. Once they start, they'll never stop."

Not surprisingly, Fairfield County's real estate fraternity supports THC. Visions of sugarplums dance in their heads at the thought of all that property to sell. Says one broker: "Builders are going out of their minds trying to find property. If Hydraulic were to put something on the market, they could get almost any price they wanted."

Small wonder that after more than a decade of dozing, THC's 2.8 million shares recently have perked up and are trading at close to $35 per share, up 50% from a year and a half ago. The land could be worth $35 a share.

What if Connecticut authorities choose not to see things THC's way? Investors could do a lot worse than sit with a stock paying 6% annually, waiting for the economic pressures of real estate development to build like water pressure behind a dam. ■

Hidden values

THC is not the only water company with good real estate in its balance sheet.

Holding company	Exch	52-week high	52-week low	Recent price	Estimated acreage
Consumers Water	O	37	27	34	19,500
The Hydraulic Co	N	37	26¼	33½	20,000
General Waterworks	O	22	17⅛	19½	5,100
JWP, Inc	O	27½	7¾	20⅜	200
Pennichuck Corp	O	NA	NA	54	2,000
SJW Corp	A	40⅞	29¾	39	7,100
United Water Res	N	22⅝	11½	20¾	7,000
York Water Co	O	NA	NA	45	1,700

NA: Not available.

It's tulip bulb time in Hollywood. No, not the flowers. The entertainment stocks.

What? Quit show business?

By Alex Ben Block

FELLOW GOES TO his doctor. "Doc," he complains, "I can't get rid of this stench that's always with me." Doctor asks patient what his job is. "I work for the circus. Clean up after the elephants." Doctor suggests patient find a new job.

"What? Quit show business?"

Now even Wall Street has caught the glamour of show business. A decade ago, aside from a handful of large studios, hardly any movie or TV production companies were public—and even those were considered pretty dicey investments. Today you can scarcely give an oil stock away, and other once-prime investments are also in the doghouse, but movie and television stocks are hotter than Rambo.

Consider the prices paid over the past two years for entertainment companies: MCA, which owns Universal Studios, has jumped 75%; Walt Disney, under new management, has rocketed 356%; and the Cannon Group is up 131%.

Now investors are turning to smaller companies, which have been going public at a record pace. Barris Industries, which recently returned to the TV-syndication market, is up 660% over two years ago; during the same period King World Productions, distributor of the *Wheel of Fortune*, has escalated 780%. New World Pictures is up 400% since January, All American Television has nearly doubled since going public eight months ago, Peregrine Entertainment is up over 500% in a year. And De Laurentiis Entertainment Group rose one-third in a month after going public in May.

Yes, it's tulip bulb time again, and anything to do with movies is in bloom. "Investors perceive the fundamentals of the entertainment business have changed," says Mark Manson, who follows show business for DLJ Securities. "The development of markets like pay-TV and home video have made their revenues much more quantifiable and reliable."

Wall Street exposes movie development

Production companies are going public at an unprecedented rate to take advantage of investors' perception that the growth of ancillary markets has lowered the risk of making movies.

Company/headquarters	Exch	Date went public	Initial offering price	Recent price	Shares† (millions)	% held by insiders	Latest 12-month revenues (thou)	Latest 12-month EPS	Primary business	Best-known product
De Laurentiis Entertainment Los Angeles	a	May '86	12	15	9.3	70%	$7,600	($0.20)	movie prod/ distribution	*Raw Deal*
Foxmoor International Films Denver	o	Oct '83	¼	½	17.7	51	8	(0.25)	movie develop	*Haunted Summer*
Kings Road Entertainment Los Angeles	o	Sept '85	10	5⅞	4.7	46	14,000	(1.14)	movie develop/ production	*All of Me*
Laurel Entertainment New York	o	June '80	3¼	7¼	2.5	31	3,200	(0.33)	tv/movie develop & production	*Tales from the Dark Side*
Mercury Entertainment Los Angeles	o	Sept '84	6*	8⅛*	14.9	46	667	(0.01)	movie develop/ production	*Flamingo Kid*
New Century Entertainment New York	o	June '82	1	4¼	14.0	41	10,400	0.02	movie develop	*To Live and Die in L.A.*
New Star Entertainment Beverly Hills	o	June '86	2*	3½*	8.7	54	400	0.01	tv/movie develop	*The Flight of the Navigator*
New World Pictures Los Angeles	a	Oct '85	7½	17	14.5	46	12,400	0.50	tv/movie/video distribution	*Angel*
Paul Entertainment Los Angeles	o	May '85	1/20	1½	12.5	75	0	0	movie develop/ distribution	*Never Too Young to Die*
Vista Organization Ltd New York	o	Aug '84	6¼*	75*	18.9	52	740	(0.09)	movie develop/ distribution	*Fright Night*

*Units. †Outstanding. a: American Stock Exchange. o: Over-the-counter.

Typical Wall Street chatter that: Stocks go up, and analysts find reasons. Here's another: Entertainment is one of the few American industries that has not only survived foreign competition but has actually improved its position in the world market, notes Jonathan Taplin, a former movie producer now partnered in First Media, a new Los Angeles-based entertainment investment banker.

As industrial smokestacks have cooled, real estate syndications have gone sour and high tech has fallen out of favor, says Taplin, huge pools of capital have been looking for new opportunities. At the same time a new breed of short-memoried money managers and research analysts has arrived on Wall Street and instinctively moved toward what it grew up with and knows best—TV and movies.

Alan Dorow/TB Pictures

Vista's Herb Jaffe, Gabriel Katzka and Seymour Malamed
The Blechs' handpicked team is well-funded but unproven.

The trigger for an end to the boom could be a glut of movies and syndicated TV programs. That could result from overproduction caused by an influx of eager and naive capital.

"We're going toward a point where there's too much product, and some of the smaller companies have to lose out," says Harold Vogel, show business analyst with Merrill Lynch Capital Markets and author of *Entertainment Industry Economics*. "When those promoting these companies talk about the ancillary market eliminating risk, they usually forget that, beyond production costs, there are releasing expenses such as marketing and distribution costs to be covered that can add another two-thirds to the cost," says Vogel. "Those rushing in forget the history of the movie business. When things get tough, it's very difficult to carry overhead costs."

Vogel expects to see the demand for syndicated TV programs—old shows and movies licensed to local stations—peak by the middle of next year. And within two to three years he expects a lot of small movie development companies and

The selling of the television syndicators

Old TV shows and creating original programs for ad hoc networks of independent stations are growth industries, thanks to a huge increase in the ranks of broadcasters without any network affiliation.

Company/headquarters	Exch	Date went public	Initial offering price	Recent price	Shares† (millions)	% held by insiders	Latest 12-month revenues (thou)	EPS	Primary business	Best-known product
All American Television New York	o	Dec '85	7½	13	1.9	65%	$ 7,000	$0.30	tv syndication	*America's Top Ten*
Barris Industries New York	o	Oct '68	9½	24	9.1	34	30,000	0.80E	tv production/ syndication	*Newlywed Game*
Donny Osmond Entertainment Santa Ana, Calif	o	Jan '85	5	1¾	1.2	33	0	(0.08)	tv production/ syndication	*Donny and Marie*
Tries Entertainment Los Angeles	a	Jan '84	10	8	5.2	58	25,900	0.52	tv/movie/video prod/syndic	*Tough Love*
Heritage Entertainment Los Angeles	a	Jan '69	3	9½	3.2	19	10,600	0.74	tv syndication	*Flipper*
King World Productions New York	o	Dec '84	5	44	10.2	60	81,200	1.02	tv production/ syndication	*Wheel of Fortune*
Peregrine Entertainment Ltd Los Angeles	o	Apr '81	4	26	1.5	45	6,500	(0.82)	tv production/ syndication	*Dancin' to the Hits*
Reeves Communications New York	o	Feb '80	9	11½	12.5	21	93,100	0.73	tv production	*Kate and Allie*
Republic Pictures Corp Los Angeles	o	Dec '84	3½	13½	3.8	31.5	15,000	0.26	tv/video syndication	*Get Smart*
Satori Entertainment New York	o	Dec '84	5*	2*	3.2	69	3,200	0.01	tv syndication	*Riddle of the Sands*

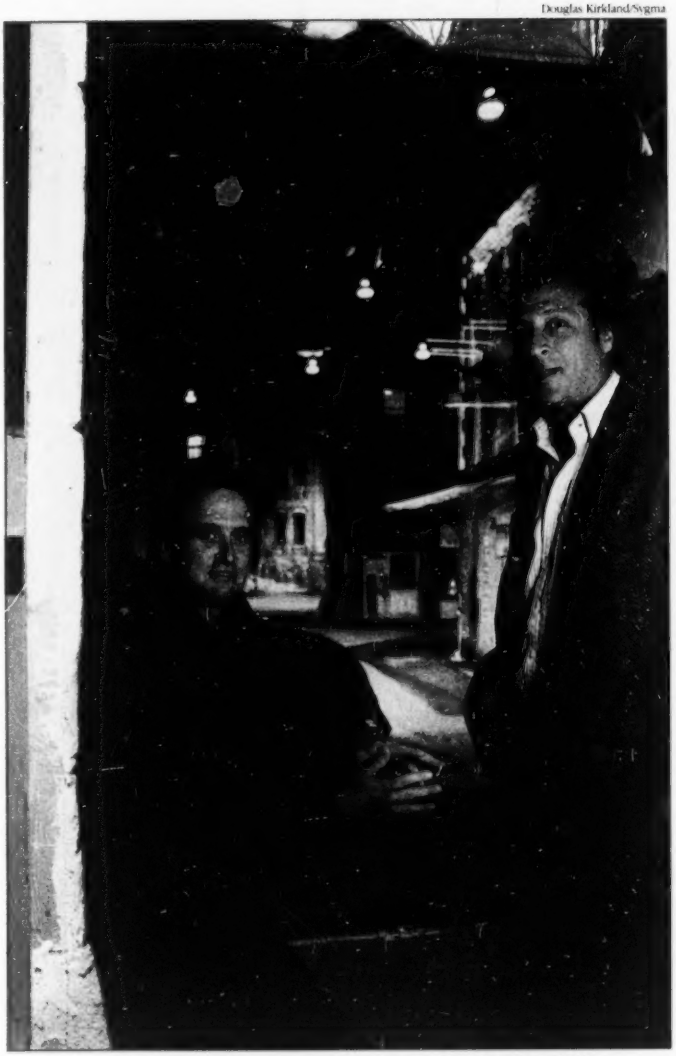
*Units. †Outstanding. a: American Stock Exchange. o: Over-the-counter.

distributors will disappear because more movies are being produced than the market can handle. "An awful lot of people are fooling themselves," says analyst Vogel.

But when the naive money pours in, there are always smart people around to garner it. One of those cashing in is Aaron Spelling, the pipe-smoking producer of such sweet-and-sour concoctions as *Dynasty, The Love Boat* and *Hotel.* In a deal scheduled to close early this month Spelling was to sell about a quarter of his company for around $130 million, with nearly $100 million going directly into his own pocket. While Spelling's credits as a producer are many, the list of properties included in the company is short. Rights to many early Spelling hits, such as *Charlie's Angels* and *Fantasy Island,* have already been sold off.

Investors will bite in the belief that Spelling, who hopes to launch his first successful half-hour sitcom in many years this fall on ABC, with Lucille Ball, can rebuild his inventory of hits and then enter TV syndication on his own for the first time.

Douglas Kirkland/Sygma



Mercury Entertainment's Michael Douglas and Michael S. Phillips
Their partnership provided new clout and pushed up the stock.

There is even more magic and less substance in a deal being offered by talented actor/director Ron Howard *(Cocoon),* former star of *Happy Days,* and his producer/partner Brian Grazer *(Spies Like Us),* who together made the 1983 hit *Splash.* Howard, 32, and Grazer, 34, are selling 34% of Imagine Productions for $13 million through Allen & Co. Imagine Production's business? Leasing out the services of its two principals and then slowly expanding into developing movies and TV shows. The stock is offered at $7. Book value: 1 cent.

Imagine isn't the first producer to turn to Wall Street. Former attorney and securities analyst Michael S. Phillips became a producer in 1971 with *Steelyard Blues,* and then hit it big in 1974 with *The Sting.* He was flying high when he took Mercury Entertainment public in September 1984. Mercury raised almost $4 million by selling just over 30% to the public, in $6 units, in an underwriting by Muller & Co. The offering was oversubscribed, even though Phillips hadn't had a hit since *Close Encounters of the Third Kind* in 1977.

The Mercury prospectus seemed to promise a practically risk-free deal. All operating and development costs were to be covered under an agreement with ABC Motion Pictures, while actual financing of movies would be done by major studios. Of course there are no sure things in show business. In the two years since, ABC Motion Pictures has gone out of existence and Mercury has managed to get just one movie released, *The Flamingo Kid,* which didn't do well enough to return anything beyond a producer's fee.

Now, Phillips has joined with actor/producer Michael Douglas *(Romancing the Stone* and *Jewel of the Nile),* using Mercury stock to buy the rights to films owned by Douglas, including Oscar winner *One Flew Over the Cuckoo's Nest.* Douglas' involvement, and the clout it is expected to provide, has helped push the price of the units up above $8.

Another firm, The Vista Organization Ltd., started out two years ago to be a movie development company like Mercury. After its first two movies performed poorly, Vista returned to Wall Street and raised an additional $69 million to enter movie distribution and home video. Despite the failure of its films *(Fright Night* and *The Falcon and the Snowman),* Vista units, which came out at $6.25 each in 1984, have sold as high as $105 and recently were $75.

Vista itself is quite a production. It was assembled by David and Isaac Blech, brothers who have had success with biotech companies. The Blechs operate by picking an area they want to be in and then contracting with top talent, whether a research scientist or a movie producer. For Vista, the Blechs' brought together former United Artists production chief Herb Jaffe, producer Gabriel Katzka *(Same Time Next Year)* and longtime Columbia Pictures financial executive Seymour Malamed. "Our goal is to build a full-fledged communications company," says David Blech. So far, mostly all talk.

The Blech brothers may find movie distribution difficult. The major studios, through long-term relationships, dominate American movie theaters. The few play-dates left are fought over by the growing legion of small distributors like Atlantic, Island and Crown International. "It's one thing when 4 or 5 small distributors compete for those few in-between play-dates," says Taplin, who produced *Baby* and

The Last Waltz. "It's a disaster when 20 companies compete."

The biggest roll of the dice these days is in original programming for TV syndication. It was uneconomical for anyone except the networks to make new programs until a few years ago, when the number of independent stations began to expand. Now everything from first-run game shows to situation comedies is being offered to the independent TV market.

But overcrowding is becoming evident here, too. George Back, 46, president of All American Television, which produces and sells first-run syndicated programs such as *America's Top Ten*, warns that of the hundreds of new shows offered to stations last year, only about 15% ever got enough commitments to go into production. And of those that made it, over 80% won't survive through a second season. "What's going on is like the bowling alley boom of the Fifties," says Neil Rosenstein, president of Peregrine Entertainment. "The mortality rate in this has got to be enormous—unless you have a solid base of repetitive assets that provide sustained business."

Let's put it this way: A lot of show business types are going to make more money selling stock than selling entertainment. And Joe Investor may well be headed for the cleaners. ■

What's the difference between selling a quick oil change and selling a Big Mac? Answer: Not all that much.

McOil Change

By John Merwin

ONE MORNING 32 years ago, milk shake machine salesman Ray Kroc stood in a parking lot in San Bernardino, Calif. eyeing a local hamburger stand owned by two brothers, Mac and Dick McDonald. Dozens of people were lining up to buy hamburgers, fries and shakes. After studying the scene for a while, Kroc figured out why: The parking lot was spotless, prices were modest, there was no waiting, the menu had only a few items, and every movement in food preparation had been studied, timed and broken down to simple steps for workers.

A veteran marketing man, Kroc knew a simple but great idea when he saw one: It was assembly-line precision applied to food retailing. Ray Kroc bought out Mac and Dick McDonald, and you know the rest.

Now shift the scene to Salt Lake City in the summer of 1986. Stand in the spotless driveway of Minit-Lube, a fast-growing auto lubrication franchise, where cars are streaming into Minit-Lube's bays, three abreast. Why is this chain so successful? Perhaps it is because, aside from the drive-through car bays, Minit-Lube looks nothing like a greasy automotive business. It's clean, painted white and surrounded by neatly trimmed, lush landscaping. Even Minit-Lube's sign carries a subtle message—the red, yellow, orange and white are the colors of McDonald's, Burger King and Wendy's. Talk about image marketing.

In fact, the place should have been named McOil Change. The customer pulls up, is greeted by a smiling employee trained to make eye contact. The customer then places the standard order—a check or fill of brake and power-steering fluids, motor oil, battery water and filters for air and oil. Thereafter, a uniformed service team springs into action. One pops the hood to check and fill fluids. Another vacuums the interior and cleans windows. A third, from a pit below, works his way along the drive shaft, grease gun and wrench in hand, lubricating joints, draining the oil and replacing the filter. Within ten minutes the driver is on his way. The bill: $20. Sears charges the same for just an oil change and lubrication, and it can take up to an hour.

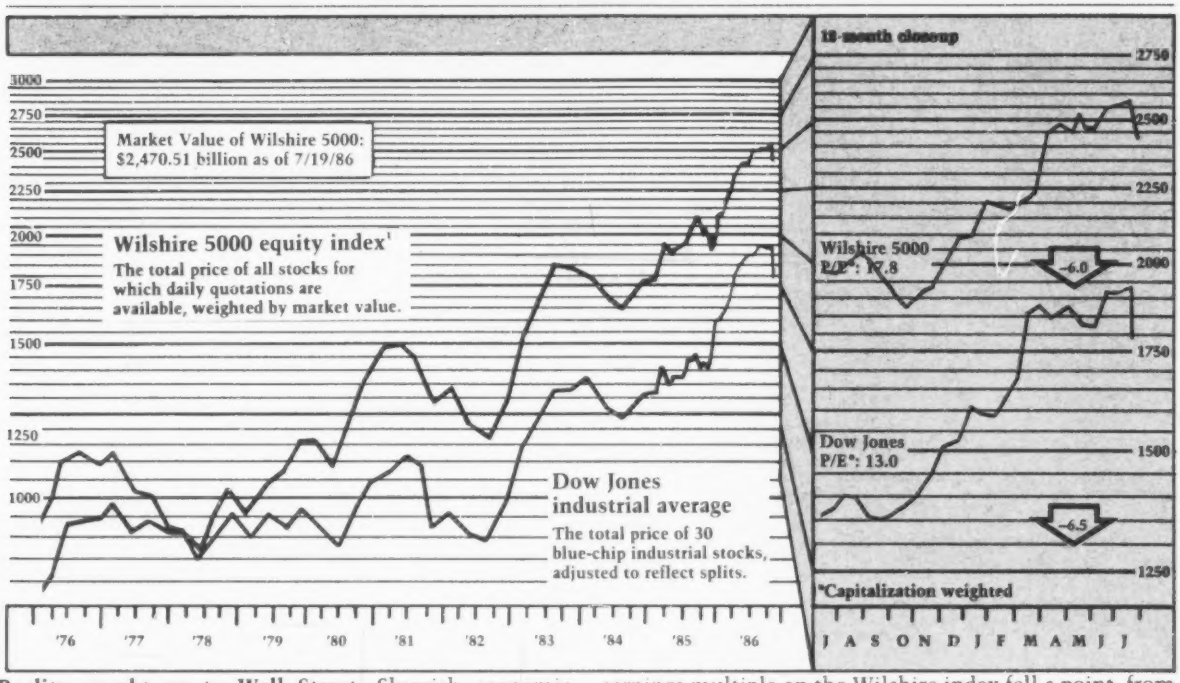
And our McDonald's analogy continues. McDonald's trains new franchisees at "Hamburger University," near Chicago. Minit-Lube trains them at a school in Salt Lake City. McDonald's rates employees in a highly publicized "All-American Team" compe-

Alejandro Tomás

A Minit-Lube service bay, Salt Lake City, Utah
The lube, oil and filter change takes ten minutes.

The Forbes/Wilshire 5000 Review

Edited by Steve Kichen



Reality caught up to Wall Street. Sluggish economic growth and disappointing corporate earnings scared some investors. Others were put off by the prospect of higher capital gains taxes next year. Whatever the cause, some handsome paper profits were converted into cash. The heaviest selloff was in Nasdaq issues, which fell 7.3% in the last two weeks. The Dow industrials finished with a 6.5% decline, while the overall market, as measured by the Wilshire index, lost 6%. Within two weeks the price/earnings multiple on the Wilshire index fell a point, from its recent peak of 18.9, to 17.8.

The Forbes Sales 500 is currently priced at 12.6 times 1986 earnings estimates and 10.8 times 1987 estimates *(see following page)*. For the last several weeks security analysts have been slashing forecasts in earnest. If estimates keep sliding, one of two things will happen: Multiples against forecast earnings will rise in order to prop up stocks at their current price levels, or share prices will fall.

Closeup On The Equity Markets

Performance of six leading indexes

Percent change	Wilshire 5000	Forbes 500[2]	Dow Jones industrials	NYSE Composite	Amex Market Value Index	NASDAQ Composite
in last 4 weeks	-3.9	-4.5	-5.4	-3.7	-5.0	-4.0
in last 52 weeks	20.6	17.9	30.8	20.4	13.0	23.8

Stock performance based on six key investor yardsticks

Percent change	Company size		Volatility[3]		P/E multiple		Dividend yield		Growth profile[4]		Share price	
	large	small	high	low	over 25	under 5	over 7.5%	none	high	low	over $40	under $4
in last 4 weeks	-3.4	-2.5	-4.2	1.3	-5.5	-1.4	0.5	-3.7	-5.2	0.6	-2.2	-3.4
in last 52 weeks	21.3	40.3	56.8	28.1	18.3	33.0	21.3	39.7	50.2	34.1	35.5	24.9

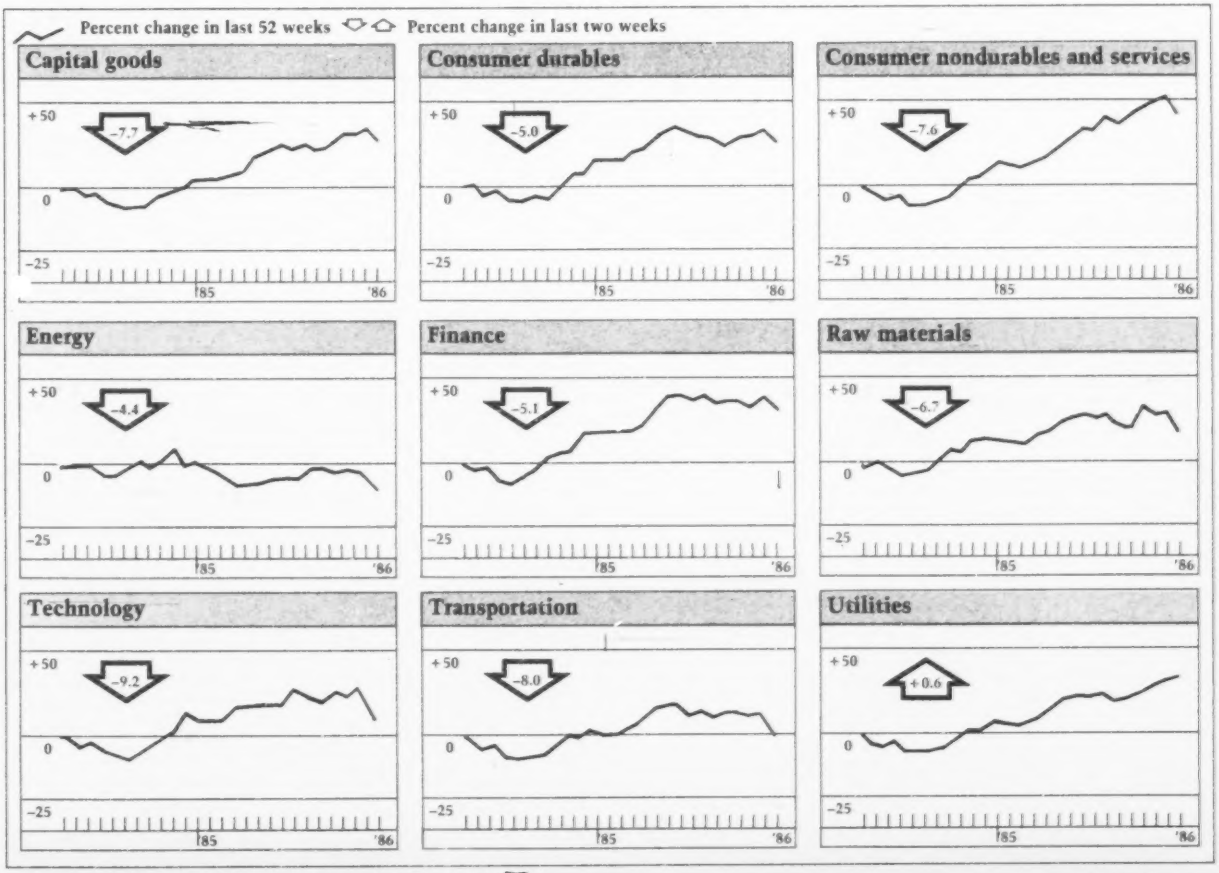
[1]Wilshire index reflects price performance. It differs slightly from market value of outstanding stocks because of retirements of equity since index was created.
[2]Based on sales.
[3]A stock's sensitivity to overall market movement. High-volatility issues have wide price fluctuations, low-volatility issues are more stable.
[4]A quantitative evaluation of a stock's growth image, determined by Wilshire Associates.

Note: All data for periods ending 7/19/86. Prepared by Wilshire Associates, Santa Monica, Calif.

Where The Action Is

Unpopularity contest. Except for the utilities, all Wilshire sectors fell out of investor favor over the last several weeks. Technology shares, with a 9.2% two-week decline, were off the most. IBM, on weak second-quarter earnings, led this group downward. IBM managed to lose more than $10 billion in market capitalization in ten trading days. Other technology issues that came under severe selling pressure include Advanced Micro Devices, Apple Computer and Burroughs.

The second-hardest-hit group was transportation, which fell 8%. The biggest losers in this sector were the airlines, thanks in large part to Texas Air, down 15%. Capital goods and consumer nondurables fared only slightly better, with losses just under 8%.



What The Analysts Think

Bottom of the barrel. Recent estimate cuts for oil stocks have not been as severe as those for most other groups. One reason is that energy estimates were drastically chopped earlier. Analysts also expect big companies that do a lot of refining to recover at the pump some of what they're losing at the wellhead.

Forecasting the Forbes 500

Performance period	Average earnings per share	P/E
latest 12 months	$2.72	16.1
1986 estimates	3.47	12.6
1987 estimates	4.05	10.8

Rank based on change in estimate	Sector	Estimated 1986 EPS	Estimated 1986 P/E	% change in 1986 estimate in 2 weeks	% change in 1986 estimate in 4 weeks
1	Utilities	$3.33	10.2	-0.08%	-0.45%
2	Energy	2.23	12.4	-0.37	-3.15
3	Consumer nondurables	2.18	16.9	-0.40	-0.76
4	Finance	3.43	11.0	-0.60	-0.98
5	Capital goods	2.59	14.4	-0.88	-2.55
6	Technology	2.53	14.1	-0.99	-1.81
7	Consumer durables	3.72	10.1	-1.11	-1.45
8	Raw materials	1.85	15.5	-1.75	-2.16
9	Transportation	1.79	14.7	-6.44	-13.11

Earnings projections are capitalization-weighted consensus estimates from over 2,000 security analysts. Data are compiled and updated continuously by the Institutional Brokers Estimate System (IBES), a service of Lynch, Jones & Ryan, a New York-based brokerage firm.

Note: All data for periods ending 7/18/86. Prepared by Wilshire Associates, Santa Monica, Calif., IBES, a service of Lynch, Jones & Ryan, New York.

NA: Not available.

A company's operating margin, often overlooked, is a better measure of management skill than is its net profit margin.

How's business?

By Michael Ozanian

SHAREHOLDERS ARE, LOGICALLY, preoccupied with the bottom line. That tells them whether management is making them richer or poorer. But shareholders who want to know the how and the why need to look a little higher up on the profit and loss statement. There they will find operating income, which, divided by revenues, yields the operating margin. "There is no more important statistic than a company's operating margin to reveal how skillful management is in controlling operating costs and raising productivity," says Stephen Leeb, editor of the Jersey City, N.J.-based *In-*

Improved operations

These companies tracked by Value Line Data Services have all improved their operating efficiency by at least a fourth since 1980. Their stocks, however, have not kept pace with the market. In part, that is because high interest or depreciation expenses can prevent operating income from showing up on the bottom line.

	Operating margin			Price		Earnings per share		
Company/industry	1980 %	1985 %	industry avg %	recent	% change over 5 yrs	1985	% change 1980-85	P/E
American Bakeries/food processing	3.5%	5.3%	9.9%	27½	67.1%	$2.06	167.5%	13.0
Apache Corp/oil producing	41.9	62.6	47.6	8⅜	–60.1	0.38	–58.2	39.9
Banner Inds/industrial services	7.9	10.8	15.2	17	11.5	1.00	6.4	10.7
Bausch & Lomb/medical supplies	18.7	24.8	16.3	37⅞	37.7	2.23	6.2	16.7
Camco/oilfield services	12.8	17.0	18.0	15¼	–3.9	1.77	88.3	10.0
Chevron/integrated oil	9.5	18.7	17.2	35¾	–8.6	4.52	–35.6	7.9
Coastal/natural gas	8.7	12.6	14.6	30	2.9	3.61	28.5	NM
Du Pont/chemical	13.9	25.8	19.0	80½	70.4	4.61	–4.6	14.1
Exxon/integrated oil	11.9	16.6	17.2	59⅛	72.0	6.46	–0.5	8.3
General Motors/auto	0.5	7.3	8.1	75½	52.5	12.28	D–P	6.3
Gulf Resources & Chem/oil producing	14.1	29.9	47.6	12¼	–46.2	5.79	78.2	3.7
Hayes-Albion/auto parts	2.0	7.5	12.0	11⅛	25.4	1.54	D–P	9.0
Kaiser Cement/cement	10.2	13.7	14.9	13⅞	–49.0	0.94	–70.3	19.5
Lamson & Sessions/machinery	3.8	6.0	11.3	3⅜	–47.1	0.04	D–P	48.2
Mattel/toys	7.8	13.9	15.7	14	75.0	1.00	NM	20.9
Texaco/integrated oil	8.2	15.2	17.2	30	–14.6	5.11	–38.5	5.8
USX/integrated steel*	8.0	13.7	8.1	19⅜	–29.2	1.71	–67.4	58.7
Westmoreland Coal/coal	5.6	8.0	14.4	23¾	–11.2	1.24	D–P	11.5
Wickes Cos/retail	5.6	11.1	8.8	5¾	–56.3	0.11	–86.1	30.3
Wyman-Gordon/aerospace	13.2	17.2	9.6	21¼	–14.1	0.18	–89.1	NM

*Formerly US Steel. NM: Not meaningful. D–P: Deficit to profit.

Sources: Value Line Data Services, FORBES.

vestment Strategist.

Why doesn't the net income figure capture managerial success? Because it reflects not only operating decisions, like what style of jeans to sell or where to locate the transmission factory, but also purely financial decisions, like how much leverage to put in the balance sheet. Moreover, a buyer of a business will be much more concerned with its operating income than with the net income. After all, the acquiring company can control leverage, interest costs and taxes by the way it pays for the purchase, but it can't instantly transform a badly managed factory into a good one.

The table on page 120 lists currently profitable firms whose operating margins have gone up by at least a fourth over the past five years but whose stock prices have significantly trailed the market. Operating income is profit from continuing operations before depreciation, interest, taxes and extraordinary items. That is, a firm's business may be sound but its reported profits weak on account of high debt, depreciation, writeoffs or taxes. For almost half of the issues listed, profits went down even as operating margins increased.

Take Wickes Cos., the Santa Monica, Calif.-based distributor of building materials. The company's operating margin doubled between 1980 and 1985. Earnings, however, shrank from 48 cents a share in 1980 to 11 cents in 1985 because of exorbitant interest and depreciation expenses. Wickes, which emerged from 2½ years in Chapter 11 last year, currently has a debt-to-equity ratio of over 225%. But its strong operating margin, says Leeb, "makes it precisely the type of company a cash-rich takeover artist would be interested in."

Can a firm have an operating margin that is too high? John Elliott, an associate professor of accounting at Cornell, cautions, "If a firm's operating margin is considerably higher than the industry average, over time it will eventually creep back toward the average"—as competitors creep in.

Westmoreland Coal's operating margin is improving—it climbed 2.4 percentage points between 1980 and 1985—but is still below the industry average of 14.4%. In 1985, despite an industry oversupply that forced it to reduce prices by 2%, Westmoreland reduced costs 8% and increased its operating margin to 8%. On the bottom line, writeoffs from mine closings buried this improvement. Analysts haven't overlooked it, however; they expect the company to earn about $2 a share next year. ■

Statistical Spotlight

Better a business that has a moat around it than a business that has to fight for survival. Trouble is that moats are getting a mite expensive these days.

Franchise mania

By William Baldwin

THE LATEST FAD WORD on Wall Street is franchise. Businesses with "franchises" are worth anything; businesses without them are just businesses.

For this phenomenon you can thank Warren Buffett, the mighty media investor of Omaha. He popularized the word as a way to explain why it's so much better to own a television network or an advertising agency than, say, an automobile plant. Now, alas, lots of very ordinary analysts parrot the word, especially when they want to justify a lofty stock price. They argue, in effect, that any company trading at a big multiple of its book value must, by definition, possess a franchise of some sort.

But what does Buffett mean by franchise? He gave a definition in a Columbia Business School seminar last year: "The test of a franchise is what a smart guy with a lot of money could do to it if he tried. If you gave me a billion dollars, and you gave me first draft pick of 50 business managers and 50 journalists, and you said, 'Go take the *Wall Street Journal* apart,' I would hand you back the billion dollars. There are some businesses that have very large moats around them. Those are the businesses you want."

To put it in popular terms: A franchise is a circumstance that gives a company some degree of monopoly pricing power. It could be a government license, a government-enforced trademark, or an economic fact of life—such as the fact that most cities won't support two newspapers, so the one that's left is sitting pretty. Buffett's Berkshire Hathaway owns the only paper in Buffalo, a franchise worth a few hundred million dollars. RJR Nabisco owns the Ritz franchise. This isn't a pure monopoly, of course—you can always buy some other cracker—but only one company is entitled to the shelf space and the consumer attention that this name brings. The name is probably more valuable than the cracker factories.

No question, a good franchise is a thing to own. The Tennessee family with the big Coca-Cola bottling franchise recently agreed to sell for $1.4 billion. Stock in Subaru of America, whose principal asset is an exclusive car-importing franchise, is up 49,100% since 1975. Pretty good, huh? But maybe it's time for investors to ask themselves if the franchise concept has been a bit overplayed. Is it possible that broadcasters, newspaper publishers, cable systems and consumer goods companies aren't worth the lavish prices that Wall Street assigns them?

Howard Fox, a portfolio manager at Carret & Co., a New York City money manager, thinks so. "This focusing on a narrow group has resulted in another Nifty Fifty—New York Times selling at 29 times earnings and so on. It's unhealthy," he says.

Another skeptic is Charles Royce, a fund manager in New York City with a preference for down-to-earth companies. (Royce Value Fund's top positions include a coal company, a coffee distributor and a lounge chair maker.) "Even dear old ABC isn't the franchise it used to be," he says, referring to a takeover that Berkshire Hathaway helped finance. "There could be

Expensive franchises

Some businesses, like Gannett's monopoly papers, are protected by what Warren Buffett calls a "moat" around them. But does it make sense to pay $70 for a moat around $5 of physical assets?

Company	Franchise	Pretax return on operating capital[1]	Aftertax return on tangible net worth[2]	Per share: tangible net worth	Per share: recent price
American Capital Management[3]	fund advisory contracts	550%	88%	$1.42	22⅛
American Home Products	drug brands	82	34	13.86	85⅞
Dow Jones[4]	newspaper	46	45	3.19	33¼
Gannett	newspapers, tv stations	60	67	4.71	74½
Kellogg	cereal brands	53	43	5.31	51½
Plenum Publishing	scientific publications	83[5]	42	10.36	65½
RJR Nabisco	cigarette and snack brands	31	NM	–0.49	51⅝
Subaru of America	car-importing franchise	76	29	5.41	30¾
Telerate	bond database	82	24	3.22	19
WD-40	lubricant brand	107	33	3.81	25¼

Data for fiscal year 1985 except where noted. [1]Income before interest, taxes and goodwill amortization, divided by debt plus equity less goodwill and excess cash. [2]Net income divided by year-end tangible net worth. [3]Data for 12 months to Mar. 31, 1986. [4]Reflects pro-rata share of Telerate tangible net worth. [5]Includes deferred subscription revenue in operating capital. NM: Not meaningful.

the potential for a fourth network, or other inroads. [Franchises] are not natural laws set down by Moses. They change over time."

In the early part of this century, traction companies that stayed in the good graces of city aldermen got lucrative exclusive franchises for their territories. In the 16th century Queen Elizabeth granted exclusive franchises to salt sellers—in effect, licenses to print money. Today's equivalent is a license from the Federal Communications Commission. Are franchises forever? Interborough Rapid Transit used to be a highflier on the Big Board. Today its assets are covered with graffiti.

This is not to say that franchises are worthless. Dow Jones is worth a lot more than its printing plants and typewriters. But is it worth $3 billion?

The table above presents a sampling of companies with franchises trading at large premiums to their tangible net worth. Tangible net worth is net worth minus the franchises—more precisely, net worth minus intangible assets like goodwill, patents and brand names. Profits are enviable; returns on tangible net worth for these companies are steep, in some cases outlandish. The only problem is that the franchise in question is not guaranteed. Someone may figure out how to get across the moat. ■

The Funds

Are big investors in funds subsidizing small ones? Some fund operators think so, and they're looking for ways to raise fees on those pesky small accounts.

Small investors, watch out

By Laura R. Walbert

SHOULD ONE MUTUAL FUND investor pay a higher percentage annual fee than another just because he has less invested in the fund? Or conversely, should larger investors get higher returns? There are rumblings in the mutual fund industry these days about allowing just that.

Traditionally, large and small fund investors have paid the same percentage advisory fee, the same percentage administrative fee, and so forth. But that's what some funds argue is so unfair. "A $10,000 account is not ten times more expensive than a $1,000 account. Yet normal mutual fund pricing structure assumes it is," says Richard Reilly, executive vice president of Fidelity Management & Research Co. Reilly says smaller accounts mean more clients and more pesky phone calls. "People who give you money expect to be talked to," he says. Reilly's solution: a management fee that scales down as the assets in an account grow.

For now, the debate centers on institutional funds where the idea is not completely new. Fidelity's Qualified Dividend Fund, solely for corporate investors with a minimum investment of $50,000, has an "advisory and service fee" that ranges from 0.78% for accounts of $50,000 to 0.48% for accounts over $2 million. Fidelity says that the bulk of the savings for larger accounts comes from the so-called transfer agent fee, for shareholder accounting.

The argument makes some sense. Most funds pay a flat fee per account to the fund's transfer agent, say $20 a year, regardless of account size. In a fixed-percentage fee scale, that might translate to a charge of 0.2%. So the